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HAROLD B. WILLEY,

IN THE

Supreme Court of the United States

OCTOBER TERM, 1954

No. 630

BARD-PARKER COMPANY, INC., *Petitioner,*

v.

COMMISSIONER OF INTERNAL REVENUE, *Respondent.*

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

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To the Honorable Chief Justice and Associate Justices of the Supreme Court of the United States:

The petitioner, Bard-Parker Company, Inc., prays that a writ of certiorari be issued to review the decision of the United States Court of Appeals for the Second Circuit in the above case.

OPINIONS BELOW

The findings of fact and opinion of the Tax Court of the United States are reported at 18 T.C. 1255. A copy thereof is included in the record below (R. 3-14). The

opinion of the United States Court of Appeals for the Second Circuit is not yet reported. A copy thereof is appended (App. 6).

JURISDICTION

The judgment of the United States Court of Appeals was entered December 6, 1954 (R. 69). Jurisdiction of this Court is invoked under 28 U.S.C. Section 1254 (1), 62 Stat. 928.

QUESTIONS PRESENTED

With the ultimate object of determining the petitioner's basis for invested capital purposes of property paid in for its capital stock, the following questions are presented:

1. Where, pursuant to a preconceived plan, the liquidating directors of a dissolved predecessor corporation transferred all of its properties, and, concurrently, certain individuals transferred other properties and cash, to the petitioner for its capital stock, preferred and common, may such interdependent transfers be treated separately for Federal tax purposes, one transfer constituting a tax free exchange under Section 112 (b) (4), and the others taxable exchanges for failure to meet the requirements of Section 112 (b) (5), of the Revenue Act of 1928?

2. In any event, did the transfer of the properties of the dissolved corporation meet the requirements of Section 112 (b) (4)?

3. Do services constitute "property" within the meaning of Section 718 (a) (2) of the Internal Revenue Code?

STATUTES INVOLVED

The pertinent provisions of the applicable statutes are set forth in the Appendix, as follows:

Internal Revenue Code (26 U.S.C., 1946 Edition), Sections 113 (a) (7) and (8), 718 (a) (2) (App. 1-2).

Revenue Act of 1928 (c. 852, 45 Stat. 791) Sections 112 (b) (4) (5), 112 (i), 112 (j), 701 (a) (1) (App. 2-3).

Stock Corporation Law of New York, Sections 22, 29, 69 (App. 3-6).

STATEMENT OF THE CASE

Bard-Parker Company, Inc. (hereinafter referred to as the "old company") was organized under the laws of New York in 1916. Its authorized capital stock of $10,000 consisted of 80 shares of 7 per cent non-voting preferred stock of $50 par value and 120 shares of $50 par value common stock. Twenty shares of common stock were issued for cash; the remainder were issued for patents and patent applications upon detachable-blade surgical knives invented and owned by Morgan Parker. The preferred stock was donated back to the corporation where it was held as treasury stock. Morgan Parker became the sole stockholder of the old company in 1923, and in 1925 he sold 30 shares of common stock to James White, retaining for himself the remaining 90 shares. An agreement, hereinafter referred to as the "Syndicate Agreement" was entered into on July 28, 1927, between Morgan Parker, the old company and other persons referred to as "subscribers". A plan was formulated whereby detachable blade scissors invented by Morgan Parker would be produced in a limited quantity by the old company which had been engaged in the manufacture and sale of detachable knife handles and blades to determine the best method of production and the probable commercial market. It was contemplated that a corporation would be organized to manufacture the scissors. The stock in the new corporation was to be issued for the scissors patents except for the required number of shares issued for cash for organizational purposes. All the preferred and 20 per cent of the common were to be donated back to the treasury. Morgan Parker was to receive ¼ of the remaining 80 per cent of common stock, a similar portion was to be given to the subscribers, and ½

to the old corporation. Morgan Parker agreed to convey to the prospective corporation all of the scissors Patents and improvements thereon. The old company agreed to authorize the issuance of 7 per cent preferred stock of $100 par value to be sold to the subscribers and to use the proceeds in a special fund for the development of the scissors. The subscribers were given the election of converting their preferred shares into stock of the prospective corporation. The Certificate of Incorporation of the old company was amended to allow authorization of $50,000 of 7 per cent non-voting preferred shares of $100 par value and to permit the old company to acquire stock in the contemplated corporation. (R. 3-4)

Subscriptions to the preferred stock of the old company aggregating $50,000, were made by the subscribers, persons not previously interested in the old corporation. In 1928, J. W. B. Ladd was employed by the old company as a mechanical engineer and he engaged in inventive work upon the scissors resulting in improving patents issued to Morgan Parker and himself. In March, 1930, the development work had reached the stage where manufacturing could begin, but it was decided that the initial commercial venture would be in the small field of surgical scissors. It appeared advantageous commercially and economically to have the new corporation market the scissors under the name of the old corporation. (R. 4)

Accordingly, the stockholders of the old corporation, at a special meeting, expressed their desire to dissolve the old corporation and to sell the assets and distribute the proceeds. They passed resolutions on March 12, 1930, consenting to the formation of a new company of the same name and the dissolution of the old company, 15 days thereafter, as provided by Section 22 of the Stock Corporation Law of New York. It was also resolved to have the directors sell the assets, good will and corporate name of the old company to the new corporation. Preferred stock of the new corporation was to be received for the value of

the physical assets and net worth, and common stock of the new corporation aggregating a par value of $750,000 was to be taken in payment for all other property including good will and the right to use the corporate name. The new corporation, Bard-Parker Company, Inc. (hereinafter referred to as the petitioner), was incorporated in New York on April 8, 1930. The old company was automatically dissolved on April 24, 1930. The authorized capital stock of the new corporation was $1,950,000, consisting of 4,500 shares of $100 par value 7 per cent cumulative preferred and 150,000 shares of $10 par value common stock. The petitioner, through its directors, purchased the tangible assets of the old company from the liquidating directors of that corporation on April 28, 1930, for $209,300 par value preferred stock and the assumption of liabilities of $18,855.59. The intangible assets of the old company were purchased for $750,000 par value common stock of the petitioner. The memorandum of agreement states that the old company had been dissolved. (R. 5)

The liquidating directors of the old company listed the shareholders of that corporation and the number of preferred and common shares to be issued to each in payment of the tangible and intangible assets of the old company. The preferred shareholders of the old company received $50,000 par value in preferred shares of the petitioner. The remaining $159,300 of the purchase price of the tangible assets was paid to the common stockholders of the old company in the ratio in which they owned stock of their corporation, 75 per cent or $119,475 par value to Morgan Parker and 25 per cent or $39,825 par value to James White. The common stock of the new corporation was issued in the same ratio, $562,500 par value to Parker and $187,500 par value to White. (R. 5-6)

On the same date the directors of the petitioners authorized the purchase of certain patents and applications covering detachable blade scissors, accepting an offer made by Harry B. Arden. These patents and applications pur-

chased by the petitioner for $750,000 through Arden were owned by Morgan Parker. Arden, in completing the transaction, listed the persons to be issued the $750,000 par value of common stock in exchange for the patents. The reason for issuing the stock to others than the owner of the patent was said to be to induce those other persons to finance the syndicate. The subscribers to the $50,000 par value of the old company preferred stock were to receive 15,000 shares in this transaction. Morgan Parker was to receive 33,750 shares and James White was to receive 11,250 shares. Frederic Bard, an attorney who acted for the syndicate, was to receive 14,750 shares as part of this transaction for the patents. Eugenia E. Ehnen, Frederic Bard's secretary, was to receive 250 shares. Frederic Bard retained only 4,000 shares of common stock, 750 shares being transferred to Morgan Parker, 1,500 shares to J. W. B. Ladd, and 8,500 to the petitioner's treasury. Additional capital was obtained by petitioner through the installment sale for cash of $101,000 par value preferred stock principally to the original subscribers for preferred stock of the old corporation. Included in these sales were purchases by J. W. B. Ladd and the Crescent Manufacturing Company, who were not original subscribers. Gain or loss was not reported by petitioner or Morgan Parker from the transactions involving the purchase by petitioner of the old company's assets and Morgan Parker's patents. (R. 6)

J. W. B. Ladd received $50,000 par value in common stock of the petitioner for his services resulting in improvements to the detachable blade scissors. An amendment of petitioner's charter reducing the authorized preferred stock from 4,500 to 4,000 $100 par value shares and increasing the authorized common stock from 150,000 to 155,000 $10 par value shares, was made in order to make this distribution possible. (R. 7)

In its excess profits tax returns for the years 1941 to 1944, inclusive, the petitioner included in its invested cap-

ital the full par value of its common stock which the respondent, in his notice of deficiency eliminated, thereby determining deficiencies in excess profits taxes for each year. (R. 3)

The Tax Court sustained the Commissioner in holding that the $750,000 common stock issued for the intangible assets of the old company was a reorganization transaction within the meaning of Sections 112 (b) (4) and 112 (i) (l) (B) of the Revenue Act of 1928, and, accordingly, that Section 113 (a) (7) of the Internal Revenue Code limited the basis to that of the transferor (R. 11). It also sustained the Commissioner in holding that no portion of the $50,000 common stock issued to Mr. Ladd for services was includible in invested capital since services constitute "neither money nor property" within the meaning of Section 718 (a) of the Code (R. 9). The appeal to the Second Circuit was limited to a review of the Tax Court's holding in these two respects.[1]

As to the other $750,000 common stock which was issued at the same time for the scissors patents, the Tax Court disapproved the Commissioner's determination for failure to qualify under Section 112 (b) (5) of the 1928 Act. It found the value of said patents and held such value was properly includible in petitioner's invested capital. (R. 14) Neither side appealed from this holding.

The Second Circuit affirmed the decision of the Tax Court (R. 67, 69). It rejected as untenable the petitioner's contention that the transaction as a whole should have been tested only under Section 112 (b) (5) to determine whether it was nontaxable (R. 62). It held that, on the facts of this case, "there occurred (1) a tax-free reorganization exchange of the old company's intangible assets for new company stock plus (2) a separate non-reorganization exchange of the patents for such stock." (R. 66)

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[1] There is no issue as to the preferred stock issued by petitioner. See Exhibit 36 (R. 43) for a summary of all stock issued and the consideration received therefor.

SPECIFICATION OF ERRORS TO BE URGED

The Court of Appeals for the Second Circuit erred:

1. In holding that concurrent and interdependent transfers of property to the petitioner in exchange for its common stock were severable for tax purposes, and that one of said transfers involved a nontaxable transaction notwithstanding the other was held to be taxable.

2. In holding that Section 112 (b) (4) of the Revenue Act of 1928 had any application in the instant case.

3. In failing and refusing to hold that since there were interdependent transfers by two or more "persons", the transaction as a whole should have been tested, as to its taxability, solely under Section 112 (b) (5) of said act.

4. In holding that invested capital may not include any amount representing capital stock issued for services.

REASONS FOR GRANTING THE WRIT

I. The Decision Below Conflicts With Decisions Holding That Interdependent Parts of a Single Transaction Are Not Severable for Tax Purposes

It is a well established principle that the individual parts or steps in a unitary transaction may not be treated separately for tax purposes. The parts of a reorganization must be considered as a whole rather than separately. *Helvering* v. *Alabama Asphaltic Limestone Co.*, 315 U.S. 179;[2] *Riddlesbarger* v. *C. I. R.* (CA-7), 200 F.2d 165. "A single transaction may not be broken up into various elements to avoid a tax." *Ahles Realty Corp.* v. *C. I. R.* (CA-2), 71 F.2d 150, 151, cert. den. 293 U.S. 611; *Bassick* v. *C. I. R.* (CA-2), 85 F.2d 8, 10, cert. den. 299 U.S. 592; *West Texas Refining & Development Co.* v. *C. I. R.* (CA-10), 68 F.2d 77; *Prairie Oil & Gas Co.* v. *Motter* (CA-10), 66 F.2d 309; *May Broadcasting Co.* v. *United States* (CA-8), 200 F.2d 852.

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[2] Cited by the Tax Court in the instant case (R. 11).

American Bantam Car Co. v. *C. I. R.* (CA-3), 177 F.2d 513, cert. den. 339 U.S. 920, affirmed per curiam the Tax Court decision, 11 T.C. 397. There (at page 405) the Tax Court stated the question thus:

> An important test is that of mutual interdependence. Were the steps so interdependent that the legal relations created by one transaction would have been fruitless without a completion of the series?

Notwithstanding in the instant case the Tax Court found that the separate transfers were interdependent,[3] it accorded separate treatment to the two transfers, with a hybrid result, and the Second Circuit affirmed.

The fallacy of the opinion of the Court below is apparent from the following excerpt (R. 64-65):

> There were two separate transfers which did not become transmuted into *component steps of a single transfer* merely because separate properties were transferred at the same time to one transferee. These two transfers were not—as in the case of the transfer by the old company to its liquidating directors and the re-transfer by them to the new company—*mere "procedural" steps towards the completion of one transaction.* (Emphasis supplied)

The petitioner never has contended that the two transfers were steps "of a single transfer" nor that they were mere "procedural" steps. It has always contended that the two transfers, while separate, were so interdependent as to require that they be considered together, instead of

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[3] The Tax Court opinion, at page 1260 (R. 11) reads: "The principal reason for the entire transaction was the exploitation of the scissors patents. The dissolution of the old company was but a step in the preconceived plan to bring about the manufacture and sale of the knives and new scissors under the name of Bard-Parker." The old company had never owned the scissors patents. They were transferred to the petitioner "at the same time" (R. 11) that the petitioner acquired the properties of the old company.

separately. Section 112 (b) (5) is specially designed to test the taxability of transfers by two or more "persons" whether such person be an individual, a trust or estate, a partnership, or a corporation.

The decision below is clearly in conflict with the decided cases in holding (R. 66) that "there occurred (1) a tax-free reorganization exchange of the old company's intangible assets for new company stock plus (2) a separate non-reorganization exchange of the patents for such stock."

The opinion below, referring to the 1928 Act, states "Section 112 (b) (4) and (5) are cumulative, not mutually exclusive." It cites *Helvering* v. *Cement Investors, Inc.*, 316 U.S. 527, 533-534, which involved the Revenue Act of 1936 (49 Stat. 1648, 1678, c. 690). Speaking through Mr. Justice Douglas this Court there stated (p. 534):

> The close relationship between § 112 (b) (5) and the "reorganization" provisions is further evidenced by the fact that they overlap to a degree. Thus a transaction which meets the requirements of clause B or clause C of § 112 (g) (1) may also qualify under § 112 (b) (5).

Disregarding the effect on this language of the differences between § 112 (g) (1) of the 1936 Act and § 112 (i) (1) of the 1928 Act,[4] nothing short of a distorted construction would support the conclusion that (b) (4) and (b) (5) are "cumulative" to the point that "a transaction" may be severed into its parts, with the grotesque result that one part was nontaxable under (b) (4), and the other part was taxable for failure to meet the requirements of (b) (5). Obviously, the Second Circuit's reliance on *Helvering* v. *Cement Investors, Inc., supra,* is misplaced.

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[4] See distinction noted in *Helvering* v. *Southwest Consolidated Corp.*, 315 U.S. 194, at p. 198.

II. The Decision Below Refuses to Follow the Decision of Another Circuit, and Is Otherwise Opposed to the Authorities Dealing With the Application of Section 112 (b) (4).

Under comparable facts and circumstances (insofar as the transfer of properties of the old company was concerned), *United States* v. *Arcade Co.* (CA-6), 203 F. 2d 230, cert. den. 346 U.S. 828, held that Section 112 (b) (4) of the Internal Revenue Code (similar in this respect to Section 112 (b) (4) of the 1928 Act) could not apply because the old company had been dissolved prior to the transfer, and, therefore, there could be no compliance with the "strict language of the statute" as to a transfer by the old corporation, nor were there any agreements between the old and new corporations, or exchanges between them, pursuant to a plan of reorganization.[5] It also noted that Treasury Regulations 103, Sec. 19.112 (g)-6 requires that the "plan of reorganization must be adopted by each of the corporations parties thereto; and the adoption must be shown by the acts of its duly constituted responsible officers and appear upon the official records of the corporation."

In footnote 3 of the opinion below (R. 63), the Second Circuit refuses to follow the *Arcade* decision, *supra.*

Apart from the technical reasons advanced in the *Arcade* opinion, there are other cogent reasons why Section 112 (b) (4) should not apply in the instant case. By its plain terms there must be an exchange of property (1) by a corporation[6] (2) which is a party to a reorganization[7] (3)

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[5] At pp. 232-233.

[6] Note the singular "a corporation".

[7] There was no reorganization under Section 112 (i) (1) (B), relied upon by the respondent, since the requirement as to 80% control by the old corporation or its stockholders (as such stockholders) was lacking—this for the reason that at the same time $750,000 common stock was issued by petitioner to acquire the scissors patents.

in pursuance of a plan of reorganization[8] (4) solely for stock or securities in another corporation (5) which is a party to the reorganization.[9] Unless all of these elements are present, Section 112 (b) (4) can have no application. The "reorganization" provisions are restricted to intercorporate transactions, but § 112 (b) (5) is not so confined. *Helvering* v. *Cement Investors, Inc.*, 316 U.S. 527, 533.

It is not mere happenstance that from the decided cases we find implied acceptance by the Commissioner and by the Courts of two propositions:

1. Where Section 112 (b) (4) (or its counterpart) was successfully invoked, (a) the reorganization was the whole transaction, not merely a part of it, and (b) there was only one transfer.[10]

2. In other transactions involving transfers of property for capital stock of a corporation, including transactions in which one or more of the transferors were corporations, the sole test used for recognizing taxable gain was that laid down in Section 112 (b) (5), or its counterpart.[11]

Had the transfer of assets of the old company for petitioner's stock been the entire transaction, it clearly would have been a reorganization exchange under (b) (4), and

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[8] There was no plan of reorganization. The only plan of any kind was that set forth in the Syndicate Agreement of July 28, 1947 (R. 47) as modified to include the purchase by petitioner of the assets of the old corporation.

[9] See footnote 8.

[10] *Helvering* v. *Alabama Asphaltic Limestone Co.*, 315 U.S. 179; *Palm Springs Holding Corp.* v. *C. I. R.*, 315 U.S. 185; *John A. Nelson Co.* v. *Helvering*, 296 U.S. 374; *Helvering* v. *Minnesota Tea Co.*, 296 U.S. 378.

[11] *United Carbon Co.* v. *C. I. R.* (CA-4), 90 F. 2d 43; *C. I. R.* v. *Lincoln-Boyle Ice Co.* (CA-7), 93 F. 2d 26; *Budd International Corp.* v. *C. I. R.* (CA-3), 143 F. 2d 784, cert. den. 323 U.S. 802; *Hartford-Empire Co.* v. *C. I. R.* (CA-2), 137 F. 2d 540, cert. den. 320 U.S. 787.

there would have been no controversy. But when the Court below held that "there occurred (1) a tax-free reorganization exchange - - - - *plus* (2) *a separate non-reorganization exchange of the* [scissors] *patents* for such stock (emphasis supplied) (R. 66), then, consistent with the imposing weight of authority, *supra,* it should have ruled out (b) (4), and tested the entire transaction under (b) (5). As it is, the decision below stands as an isolated case without precedent.

III. The Intervention of This Court Is Warranted to Clarify the Scope and Application of Subsections (4) and (5) of Section 112

United Carbon Co. v. *C. I. R.* (CA-4), 90 F.2d 43, has long been regarded as a leading case, and has been consistently followed, in principle, by other courts. See *Blair* v. *C. I. R.* (CA-2), 91 F.2d 992, 995; *C. I. R.* v. *Lincoln-Boyle Ice Co.* (CA-7), 93 F.2d 26; *Budd International Corp.* v. *C. I. R.* (CA-3) 143 F.2d 784, cert. den. 323 U.S. 802. In that case the taxpayer issued all of its stock to acquire the properties of 13 corporations and one partnership.[12] Section 203 (b) (4) of the Revenue Act of 1926 (corresponding with Section 112 (b) (5) of the 1928 Act) was invoked and was held inapplicable because of the disproportionate interests received by the transferors. The 1926 counterpart of Section 112 (b) (4) was not considered.

Somewhat later, the same Circuit Court in *Britt* v. *Commissioner* (CA-4), 114 F.2d 10, in a transaction growing out of that involved in the *United Carbon* case, held that although *United Carbon* was properly decided on the issue presented (203 (b) (4) of the 1926 Act), its decision would have been different if the issue had been presented under (b) (3) of that act (corresponding with Section 112 (b) (4) of the 1928 Act). It then held in the *Britt* case that as

[12] One of the twelve transferor corporations was assignee of the assets of the thirteenth corporation. The facts are more fully stated in 32 BTA 1000.

to the particular corporation there under consideration (1 of 13 involved) the transaction constituted a reorganization, citing *John A. Nelson Company* v. *Helvering*, 296 U.S. 374, and *Helvering* v. *Minnesota Tea Company*, 296 U.S. 378, as authorities. It completely ignored the factual differences between the *Nelson and Minnesota Tea* cases on the one hand, where in each case there was only one transferor, a corporation, and the transaction before it, where the transferors were 13 corporations and one partnership.

As will be noted from the foregoing citations, the other Circuits, including the Second, have consistently followed the *United Carbon* decision and ignored the *Britt* decision. The exceptions are the Court of Claims in *Nelson* v. *United States*, 107 C. Cls. 422, 69 F. Supp. 336, cert. den. 331 U.S. 846, and the case at bar.

The *United Carbon* and *Britt* decisions, both by the same Circuit Court, are irreconcilable. Where some courts rely upon one and others rely upon the other of these conflicting decisions as authorities, uncertainty in this area of tax law will persist. Only the intervention of this Court will clarify this important phase of the law, and resolve existing doubts.

IV. The Holding That Invested Capital May Not Include Any Value In Connection With Stock Issued for Services Is Unrealistic

The holding below is that the market value of stock issued to Mr. Ladd for services was properly excluded from invested capital. The State law[13] providing for the issuance of stock for "labor done" as well as for money or property actually received is waved aside as "irrelevant". Such action is unduly technical and unrealistic.

As a practical matter, whether a corporation issues stock for cash and uses the cash to pay for services, on the one hand, or issues stock directly for the services, the end result is the same. The only difference is as to form,

[13] Section 69, New York Stock Corporation Law (App. 5).

and, in tax matters substance, rather than form, controls. *Helvering* v. *F. & R. Lazarus & Co.*, 308 U.S. 252, 255; *Palmer* v. *Bender*, 287 U.S. 551.

Any building or other structure, or any equipment, represents a combination of materials and labor, and the product of the two is generally understood to be property. The services rendered by Mr. Ladd were in connection with the invention covered by the scissors patents, and presumably added to the value of the invention, thereby increasing its value as property. Only a technical, strained construction of the statute will justify the holding below.

The Court below cites *LaBelle Iron Works* v. *United States*, 256 U.S., 377, 389 and *Simmons Company* v. *Commissioner* (CA-1), 33 F.2d 75 in support of its holding that services do not constitute property (R. 67). The *LaBelle Iron Works* case simply held that appreciation in value of property does not constitute invested capital, and the *Simmons* case held that neither discount sustained nor commissions paid in connection with the sale of taxpayer's stock, was includible in invested capital. Neither case supports the holding below.

CONCLUSION

For the foregoing reasons it is respectfully submitted that this petition for a writ of certiorari should be granted.

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